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Annual Financial Reports

Chattanooga-Hamilton County Hospital Authority (d/b/a Erlanger Health System)

June 30, 2017

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

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SECTION II

FINANCIAL SECTION

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INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of
Chattanooga-Hamilton County Hospital Authority
(d/b/a Erlanger Health System):

Report on the Combined Financial Statements

We have audited the accompanying combined financial statements of the business type activities of Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) and its discretely presented component units as of and for the year ended June 30, 2017, and the related notes to the combined financial statements, which collectively comprise the Primary Health System's basic combined financial statements as listed in the table of contents.

Management's Responsibility for the Combined Financial Statements

Management is responsible for the preparation and fair presentation of these combined financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of combined financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these combined financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Primary Health System's preparation and fair presentation of the combined financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Primary Health System's internal control. Accordingly, we express no such

opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the combined financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the aggregate discretely presented component units of the Primary Health System as of June 30, 2017, and the respective changes in financial position and, where applicable, cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information: Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis (shown on pages 5 through 12), the Schedule of Changes in Net Pension Liability and Related Ratios (shown on page 50) and the Schedule of Actuarial Contributions (shown on page 51) be presented to supplement the basic combined financial statements. Such information, although not a part of the basic combined financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic combined financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic combined financial statements, and other knowledge we obtained during our audit of the basic combined financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information: Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Primary Health System's basic combined financial statements. The accompanying Schedule of Expenditures of Federal Awards, as required by the audit requirements of Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), and the Schedule of Expenditures of State and Other Financial Assistance, are presented for purposes of additional analysis and are not a required part of the basic combined financial statements.

The Schedule of Expenditures of Federal Awards and Schedule of Expenditures of State and Other Financial Assistance are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic combined

financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic combined financial statements or to the basic combined financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedules of Expenditures of Federal Awards and State and Other Financial Assistance, are fairly stated in all material respects in relation to the basic combined financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 20, 2017 on our consideration of the Primary Health System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Primary Health System's internal control over financial reporting and compliance.

Pershing Yoakley & Associates PC

Knoxville, Tennessee
September 20, 2017, except for our report
on Other Information which is dated
January 8, 2018

Management's Discussion and Analysis

MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis of Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System's financial performance provides an overview of financial activities for the fiscal year ended June 30, 2017.

Erlanger Health System (the Primary Health System) is the largest healthcare provider in Southeast Tennessee and the seventh largest public hospital nationwide. The Primary Health System maintains a number of very specialized clinical services such as Level I trauma, Level IV neonatal, kidney transplantation, a Regional Cancer Unit, a full-service children's hospital, and open-heart surgery, all of which are primarily serviced by six "Life Force" helicopters and supported by subspecialty physicians (residents, faculty and private attending physicians) located on its campuses.

OVERVIEW OF THE COMBINED FINANCIAL STATEMENTS

The combined financial statements consist of two parts: Management's Discussion and Analysis and the combined financial statements. The combined financial statements also include notes that explain in more detail some of the information in the combined financial statements.

The combined financial statements of the Primary Health System offer short-term and long-term financial information about its activities. The combined statements of net position include all of the Primary Health System's assets and liabilities and provide information about the nature and amounts of investments in resources (assets) and the obligations to the Primary Health System's creditors (liabilities). The assets and liabilities are presented in a classified format, which distinguishes between current and long-term assets and liabilities. It also provides the basis for computing rate of return, evaluating the capital structure of the Primary Health System and assessing the liquidity and financial flexibility of the Primary Health System.

All of the fiscal year's revenues and expenses are accounted for in the combined statements of changes in net position. These statements measure the success of the Primary Health System's operations and can be used to determine whether the Primary Health System has successfully recovered all of its costs through the services provided, as well as its profitability and credit worthiness.

The final required financial statement is the combined statement of cash flows. The primary purpose of this statement is to provide information about the Primary Health System's cash receipts, cash payments and net changes in cash resulting from operating, investing, non-capital financing and financing activities. The statement also provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

The analysis of the combined financial statements of the Primary Health System begins on the next page. One of the most important questions asked about the Primary Health System's finances is "Is the financial condition of the Primary Health System as a whole better or worse as a result of the fiscal year's activities?" The combined statements of net position and the combined statements of changes in net position report information about the Primary Health System's activities in a way that will help answer this question. These two statements report the net position of the Primary Health System and changes in the net position. One can think of the Primary Health System's net position – the difference between assets and liabilities – as one way to measure financial health or financial position. Over time, increases or decreases in the Primary Health System's net position is one indicator of whether its financial health is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions, regulations and new or changed government legislation.

REPORTING ENTITY

The Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) was created by a private act passed by the General Assembly of the State of Tennessee on March 11, 1976, and adopted by a majority of the qualified voters of Hamilton County, Tennessee on August 5, 1976. The Primary Health System is considered the primary governmental unit for financial reporting purposes. As required by generally accepted accounting principles, these financial statements present the Primary Health System and its component units. The component units discussed below are included in the Primary Health System's reporting entity because of the significance of their operational, financial or other relationships with the Primary Health System.

ContinuCare HealthServices, Inc., Cyberknife of Chattanooga, LLC (Cyberknife), UT-Erlanger Medical Group, Inc. (the Medical Group) and Erlanger Health Plan Trust are legally separate organizations for which the Primary Health System is either financially accountable or owns a majority interest. Accordingly, these organizations represent component units of the Primary Health System. The financial statements of Erlanger Health Plan Trust are blended with the financial statements of the Primary Health System, as the Board of Erlanger Health Plan Trust is substantially the same as that of the Primary Health System and the Primary Health System has operational responsibility.

During fiscal year 2011, Cyberknife was capitalized by contributions from the Primary Health System and certain other minority partners. Cyberknife provides radiation therapy services, specifically robotic stereotactic radiosurgical services through the use of a Cyberknife stereotactic radiosurgery system on the Primary Health System's campus. At June 30, 2017, the Primary Health System owned 51% of Cyberknife's outstanding membership units.

The Medical Group was formed on June 30, 2011 and will provide professional healthcare and related services to the public through its employed and contracted licensed physicians and other supporting healthcare providers. The Medical Group has no members; however, the Primary Health System may access the Medical Group's services. The Medical Group is currently not active.

During fiscal year 2017, ContinuCare Health Services, Inc. sold Erlanger Pharmacies to CVS Pharmacy.

KEY FINANCIAL INDICATORS

The following key financial indicators are for Erlanger Health System as a whole. They are inclusive of the Primary Health System, ContinuCare HealthServices, Inc., and the 51% controlling share of Cyberknife of Chattanooga, LLC.

- Total income before contributions for Erlanger Health System for fiscal year 2017 is $9 million compared to $25 million for fiscal year 2016.

- Total cash and investment reserves at June 30, 2017 are $104 million (excluding $108 million in capital investment funds and $50 million of funds held by Trustees or restricted by donors or others).

- Net days in accounts receivable for Erlanger Health System (utilizing a three-month rolling average of net revenue) is 57 days at June 30, 2017 compared to 56 days at June 30, 2016.

- For fiscal year 2017, Erlanger Health System recognized $20.6 million in public hospital supplemental payments from the State of Tennessee compared to $18.2 million in fiscal year 2016.

- For fiscal year 2017, Erlanger Health System recognized $10.5 million in essential access payments from the State of Tennessee compared to $10.4 million in fiscal year 2016.

- For fiscal year 2017, Erlanger Health System recognized $8.6 million in disproportionate share payments from the State of Tennessee compared to $15.1 million in fiscal year 2016.

- For fiscal year 2017, Erlanger Health System recognized $1.2 million in trauma fund payments from the State of Tennessee compared to $1.1 million in fiscal year 2016.

The required bond covenant ratios for fiscal year 2017 compared to bond requirements are as follows:

	June 30, 2017	*Master Trust Indenture*	*Bond Insurer Requirements 04 Series*
Debt service coverage ratio	3.07	1.10	1.35
Current ratio	2.27	N/A	1.50
Days cash on hand	80	N/A	65 days
Indebtedness ratio	51%	N/A	65%

The trust indentures and related documents underlying the bonds contain certain covenants and restrictions. For fiscal year 2017, Erlanger Health System met all required debt covenants.

NET POSITION

Erlanger Health System's net position for the combined Primary Health System and Aggregate Discretely Presented Component Units increased by approximately $14 million in fiscal year 2017. Our analysis focuses on the net position (Table 1) and changes in net position (Table 2) of the Primary Health System's operating activities. Discussion focuses on the Primary Health System and its blended component units.

Net position for the Primary Health System increased from $236 million as of June 30, 2016 to $247 million as of June 30, 2017. The current ratio (current assets divided by current liabilities) decreased from 2.56 in 2016 to 2.25 in 2017 for the Primary Health System.

Table 1 - Net Position (in Millions)

	June 30, 2017		*June 30, 2016*	
	Primary Health System	*Discretely Presented Component Units*	*Primary Health System*	*Discretely Presented Component Units*
Current and other assets	**$ 423**	**$ 22**	$ 444	$ 14
Capital assets	**232**	**7**	186	8
Total Assets	**655**	**29**	630	22
Deferred ouflows of resources	**13**	**-**	15	-
	$ 668	**$ 29**	$ 645	$ 22

	June 30, 2017		*June 30, 2016*	
	Primary Health System	***Discretely Presented Component Units***	***Primary Health System***	***Discretely Presented Component Units***
Long-term debt outstanding	**$ 203**	**$ 1**	$ 208	$ -
Other liabilities	**215**	**9**	197	6
Total Liabilities	**418**	**10**	405	6
Deferred inflows of resources	**3**	**-**	4	-
	$ 421	**$ 10**	$ 409	$ 6
Net position				
Net investment in capital assets	**$ 43**	**$ 6**	$ 17	$ 5
Restricted expendable	**4**	**-**	3	-
Unrestricted	**200**	**13**	216	11
Total Net Position	**$ 247**	**$ 19**	$ 236	$ 16

Days in cash decreased from 90 days as of June 30, 2016 to 80 days as of June 30, 2017 for the Primary Health System resulting from increased investment in capital.

Days in net accounts receivable for the Primary Health System were 58 days as of June 30, 2016 and 59 days at June 30, 2017, with the increase being attributed to increased volumes.

Capital assets for the Primary Health System were $232 million as of June 30, 2017. Additions for fiscal year 2017 totaled $70 million while $19 million of assets were retired or sold. Depreciation expense was $26 million for the Primary Health System. Retirement of assets reduced accumulated depreciation by $20 million in fiscal year 2017. Construction in progress was $43 million as of June 30, 2017. Included in construction in progress is the EPIC project totaling $22 million.

Long-term debt outstanding amounted to $203 million as of June 30, 2017 compared to $208 million as of June 30, 2016.

Other liabilities for the Primary Health System were $215 million as of June 30, 2017 compared to $197 million as of June 30, 2016, due in part to increased net pension liability.

CHANGES IN NET POSITION

The focus for Erlanger Health System's management team during fiscal year 2017 was to increase the Primary Health System's volumes in a number of key product lines in a flat market,

improve relationships with stakeholders, strategic capital investment, EPIC installation and improve operating efficiencies.

Table 2 - Changes in Net Position (in Millions)

	June 30, 2017		*June 30, 2016*	
	Primary Health System	***Discretely Presented Component Units***	***Primary Health System***	***Discretely Presented Component Units***
Net patient service revenue	**$ 836**	**$ 12**	$ 778	$ 11
Other revenue	**18**	**22**	15	22
Total Revenue	**854**	**34**	793	33
Operating Expenses:				
Salaries, wages and benefits	**444**	**15**	406	14
Supplies and other expenses	**197**	**19**	174	13
Purchased services	**173**	**3**	160	3
Depreciation and amortization	**26**	**1**	25	1
Total Expenses	**840**	**38**	765	31
Operating income revenues in excess of (less than) expenses	**14**	**(4)**	28	2
Nonoperating gains	**2**	8	4	(1)
Interest expense and other	**(7)**	**(1)**	(7)	-
Operating/capital contributions	**2**	**-**	-	-
Change in Net Position	**$ 11**	**$ 3**	$ 25	$ 1

Net patient service revenue for the Primary Health System increased from $778 million in fiscal year 2016 to $836 million in fiscal year 2017. Admissions for fiscal year 2017 were 38,999 compared to 35,758 for fiscal year 2016, a 9.1% increase. Observation days increased from 7,637 for fiscal year 2016 to 8,082 for fiscal year 2017, or by 5.8%. Air ambulance flights increased from 2,190 flights for fiscal 2016 to 2,272 flights for fiscal year 2017, or by 3.7%. Medicare case mix index increased from 1.87 for fiscal year 2016 to 1.91 for fiscal year 2017. Total surgical inpatients increased from 10,143 for fiscal year 2016 to 11,277 for fiscal 2017, or by 11.2%. Total surgical outpatients for fiscal year 2017 increased by 3.7% over the prior year. Total emergency room visits were 157,038 for fiscal year 2017, a 1.4% increase over fiscal year 2016. Physician practice outpatient visits have increased from 351,875 in fiscal 2016 to 428,608 in fiscal 2017, or by 21.8%.

Salaries for the Primary Health System increased from $406 million in fiscal year 2016 to $444 million in fiscal year 2017. Staffing was in concert with the increased volumes. Paid FTE's per

adjusted occupied bed decreased from 4.7 in fiscal year 2016 to 4.6 in fiscal year 2017, however, salary cost for fiscal year 2017 per hour increased by 2.9% over the prior year. Efficient productivity of operations continue to be evident even though staff is working toward the inpatient "go live" of e-chart. A 3% raise for all other eligible employees was implemented in January 2016.

Supplies and other expenses increased from $174 million for fiscal year 2016 to $197 million in fiscal year 2017. Supplies and drugs per adjusted admission for the Primary Health System decreased from $1,815 in fiscal year 2016 to $1,754 in fiscal year 2017. Increased 340B savings have reduced drug costs for fiscal year 2017.

Purchased services increased from $160 million in fiscal year 2016 to $173 million in fiscal year 2017 due in part to an increase in contracted hospitalist fees resulting from increased volumes and increased computer services costs associated with implementation of the EPIC system project.

Depreciation and amortization expense increased from $25 million in fiscal year 2016 to $26 million in fiscal 2017 due in part to opening Erlanger East in December 2016.

Interest expense of $7 million in fiscal year 2017 is comparable to the prior year.

OUTLOOK

The State of Tennessee continues to review the TennCare program (the State's Medicaid program). For fiscal years 2012 and 2013, the State passed a Hospital Coverage Fee to offset shortfalls in the State's budget for TennCare. The fee has remained intact and TennCare rates were stable in fiscal years 2014 - 2017. CMS has notified the State of their intention to change the methodology of the supplemental pools. The TennCare waiver received final approval in December 2016. This is a five-year waiver that must remain in compliance with federal law. The biggest change in the new waiver is related to supplemental pool payments to hospitals. Out-of-state Medicaid and TennCare changes would affect the Primary Health System's bottom line with TennCare and Medicaid patients representing approximately 23% of the payer mix. Self-pay patients represent approximately 7% of the charge utilization. Healthcare reform and future changes in Medicare regulations could also have an adverse effect on the Primary Health System's future operations since Medicare represents approximately 33% of the payer mix.

During fiscal year 2014, the Primary Health System was added as a participant to the Public Hospital Supplemental Payment Pool for public hospitals in Tennessee through a collaborative effort with local Mayors, State Senators and Representatives, Hamilton County Medical Society, Board members, physicians and hospital leadership. The inclusion of the Primary Health System

in the pool netted $20.6 million of additional federal funding for fiscal year 2017 and $18.2 million for fiscal year 2016. The Public Hospital Supplemental Payment Pool is part of the current CMS pool methodology discussions. Funding of $23.3 million for fiscal year 2018 was received in August 2017.

The Primary Health System recognized Essential Access payments totaling $10.4 million from the State of Tennessee for fiscal year 2017, and $10.4 million in 2016. Disproportionate share payments were not approved by the Federal government for fiscal year 2014 and funds received during 2015 were deferred until 2016 based on management's evaluation. Disproportionate share payments of $15.1 million were recorded in fiscal year 2016 compared to $8.6 million in 2017. Additionally, the Primary Health System recognized trauma funding of $1.2 million and $1.1 million in fiscal years 2017 and 2016. Payments from the State of Tennessee for the fiscal year 2017 are expected to be consistent with the fiscal year 2016. Due to the 1966 Hamilton County Sales Tax Agreement expiring in May 2011, the Hamilton County appropriations to the Primary Health System have been reduced from $3 million to $1.5 million for 2017 and 2016.

The focus of Erlanger Health System's CEO and leadership team for fiscal year 2017 has been top-line, sustainable growth, strategic capital investment, EPIC implementation, cost containment and strengthened physician relations. The strategic plans put in place this fiscal year have yielded strong positive results and enabled investment in Erlanger and the community. The health system has infused $71 million from bond sales into major growth initiatives.

Fiscal year 2017 reflected continued growth based on strategic plan and initiatives completed to date and others in the process of being completed. The surgery expansion at the main campus is a strong contributor to health system performance as is the $50 million expansion at Erlanger East, where a full-service hospital was made available for the first time to residents of East Hamilton County. During fiscal 2017, the Primary Health System implemented the ambulatory module of EPIC. The inpatient module of EPIC will be implemented in fiscal 2018. A strong team and support cast are in place; however, the complexities of the challenge are magnified as an array of programs and services and providers need to coordinate efforts to execute successfully. Competition and related market place additional challenges and risks to the mix. An effective team is in place to accelerate effective execution of this endeavor.

For FY 2018, it is anticipated that the Primary Health System will continue to realize further progress all on fronts, the opening of the Erlanger Heart and Lung Institute, the opening of the Erlanger Behavioral Health Hospital, with growth fostered by effective execution on key strategic initiatives, by new bed and surgical capacity and by physician engagement and clinical leadership. The Erlanger brand will continue to attract the attention of other providers and physician alike. We expect to see continued growth from within the service area and from outlying areas particularly as small hospitals in the region seek to align to gain access to Erlanger's "system of care."

Audited Combined Financial Statements

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Combined Statements of Net Position

	June 30, 2017	
	Primary Health System	***Discretely Presented Component Units***
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	**$ 82,900,927**	**$ 11,859,367**
Temporary investments	**3,108,980**	**6,048,721**
Patient accounts receivable, net	**134,468,077**	**2,161,233**
Estimated amounts due from third party payers	**5,801,710**	**-**
Due from other governments	**1,199,599**	**424,619**
Inventories	**16,509,567**	**359,637**
Receivable from Walker County, Georgia	**2,901,667**	**-**
Other current assets	**19,408,061**	**699,076**
TOTAL CURRENT ASSETS	**266,298,588**	**21,552,653**
NET PROPERTY, PLANT AND EQUIPMENT	**231,517,390**	**7,032,749**
LONG-TERM INVESTMENTS, for working capital	**498,014**	**-**
ASSETS LIMITED AS TO USE	**132,018,368**	**-**
OTHER ASSETS:		
Prepaid bond insurance	**551,399**	**-**
Equity in discretely presented component units	**18,339,497**	**-**
Receivable from Walker County, Georgia, net of current portion	**5,803,334**	**-**
Other assets	**12,820**	**508,597**
TOTAL OTHER ASSETS	**24,707,050**	**508,597**
TOTAL ASSETS	**655,039,410**	**29,093,999**
DEFERRED OUTFLOWS OF RESOURCES		
Deferred pension adjustments	**12,029,558**	**-**
Deferred amounts from debt refunding	**1,458,618**	**-**
TOTAL DEFERRED OUTFLOWS OF RESOURCES	**13,488,176**	**-**
COMBINED ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	**$ 668,527,586**	**$ 29,093,999**

See notes to combined financial statements.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Combined Statements of Net Position - Continued

	June 30, 2017	
	Primary Health System	***Discretely Presented Component Units***
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	**$ 79,142,994**	**$ 2,131,557**
Accrued salaries and related liabilities	**31,561,325**	**1,269,287**
Due to other governments	**424,619**	**1,199,599**
Current portion of long-term debt and capital leases	**4,686,080**	**377,820**
Other current liabilities	**2,401,304**	**3,425,676**
TOTAL CURRENT LIABILITIES	**118,216,322**	**8,403,939**
LONG-TERM DEBT AND CAPITAL LEASE OBLIGATIONS	**202,918,634**	**937,500**
NET PENSION LIABILITY	**70,000,930**	**-**
OTHER LONG-TERM LIABILITIES	**27,615,029**	**718,454**
TOTAL LIABILITIES	**418,750,915**	**10,059,893**
DEFERRED INFLOWS OF RESOURCES		
Deferred gain from sale-leaseback	**2,718,298**	**-**
TOTAL DEFERRED INFLOWS OF RESOURCES	**2,718,298**	**-**
NET POSITION:		
Unrestricted	**200,288,815**	**13,275,257**
Net investment in capital assets	**43,266,364**	**5,758,849**
Restricted expendable:		
Health plan trust	**1,637,342**	**-**
Donor restricted	**1,865,852**	**-**
TOTAL NET POSITION	**247,058,373**	**19,034,106**
COMBINED LIABILITES, DEFERRED OUTFLOWS OF RESOURCES AND NET POSITION	**$ 668,527,586**	**$ 29,093,999**

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Combined Statements of Changes in Net Position

	Year Ended June 30, 2017	
	Primary Health System	*Discretely Presented Component Units*
OPERATING REVENUE:		
Charges for services:		
Net patient service revenue	$ 835,521,971	$ 11,647,646
Other revenue	18,368,318	22,555,419
TOTAL OPERATING REVENUE	853,890,289	34,203,065
OPERATING EXPENSES:		
Salaries, wages and benefits	443,623,327	14,955,615
Supplies and other expenses	192,063,265	18,523,552
Purchased services	173,279,391	2,839,792
Insurance and taxes	4,798,860	377,367
Depreciation and amortization	26,332,521	1,238,109
TOTAL OPERATING EXPENSES	840,097,364	37,934,435
OPERATING INCOME (LOSS)	13,792,925	(3,731,370)
NONOPERATING REVENUE (EXPENSES):		
Gain (loss) on disposal of assets	(60,460)	7,941,643
Investment income (loss), net of fees	(1,300,948)	430,423
Net gain from discretely presented component units	2,874,758	-
Interest expense	(6,308,956)	(95,948)
Provision for income taxes	-	(1,561,325)
NET NONOPERATING REVENUE (EXPENSES)	(4,795,606)	6,714,793
INCOME BEFORE CONTRIBUTIONS	8,997,319	2,983,423
Operating contributions (distributions), net	(747,667)	(250,000)
Capital contributions	2,901,378	-
CHANGE IN NET POSITION	11,151,030	2,733,423
NET POSITION AT BEGINNING OF YEAR	235,907,343	16,300,683
NET POSITION AT END OF YEAR	$ 247,058,373	$ 19,034,106

See notes to combined financial statements.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Combined Statement of Cash Flows

Primary Health System	*Year Ended June 30, 2017*
CASH FLOWS FROM OPERATING ACTIVITIES:	
Receipts from third-party payers and patients	**$ 825,621,635**
Payments to vendors and others for supplies, purchased services, and other expenses	**(364,142,335)**
Payments to and on behalf of employees	**(436,498,550)**
Other receipts	**18,959,273**
NET CASH PROVIDED BY OPERATING ACTIVITIES	**43,940,023**
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:	
Contributions to other organizations, net	**(747,667)**
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:	
Acquisition and construction of capital assets, net	**(63,658,569)**
Principal paid on bonds, capital lease obligations and other	**(4,813,051)**
Interest payments on long-term debt	**(9,417,657)**
Capital contributions	**2,901,378**
NET CASH USED IN CAPITAL AND RELATED FINANCING ACTIVITIES	**(74,987,899)**
CASH FLOWS FROM INVESTING ACTIVITIES:	
Interest, dividends, and net realized gains/losses on investments	**1,658,606**
Change in temporary and long-term investments for working capital	**(12,468)**
Net cash transferred from assets limited as to use	**22,663,306**
NET CASH PROVIDED BY INVESTING ACTIVITIES	**24,309,444**
DECREASE IN CASH AND CASH EQUIVALENTS	**(7,486,099)**
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**90,387,026**
CASH AND CASH EQUIVALENTS AT END OF YEAR	**$ 82,900,927**
SUPPLEMENTAL SCHEDULE OF NON-CASH ACTIVITIES	
Capital assets accrued in payables	**$ 9,176,970**
Unrealized investment losses	**$ (2,959,554)**

See notes to combined financial statements.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Combined Statement of Cash Flows - Continued

Primary Health System	*Year Ended June 30, 2017*
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:	
Operating income	**$ 13,792,925**
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization	**26,332,521**
Pension adjustments, net	**3,933,617**
Amortization of deferred gain	**(287,915)**
Changes in assets and liabilities:	
Patient accounts receivable, net	**(11,393,234)**
Estimated amounts due from third party payers, net	**2,198,409**
Inventories and other assets	**(950,676)**
Accounts payable and accrued expenses	**6,396,357**
Accrued salaries and related liabilities	**3,191,160**
Other current and long-term liabilities	**726,859**
NET CASH PROVIDED BY OPERATING ACTIVITIES	**$ 43,940,023**

NOTE A--SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity: The Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) was created by a private act passed by the General Assembly of the State of Tennessee on March 11, 1976, and adopted by a majority of the qualified voters of Hamilton County, Tennessee on August 5, 1976. The Chattanooga-Hamilton County Hospital Authority consists of the Primary Health System and its aggregate discretely presented component units as disclosed below.

The Primary Health System provides comprehensive healthcare services throughout Hamilton and Bledsoe counties, as well as outlying areas in southeastern Tennessee and north Georgia. These services are provided primarily through the hospitals and other facilities located on the Baroness and East campuses of Erlanger Medical Center. The Primary Health System also operates other hospitals and clinics throughout the area. The Primary Health System is considered the primary governmental unit for financial reporting purposes. As required by accounting principles generally accepted in the United States of America, these combined financial statements present the Primary Health System and its component units. The component units discussed below are included in the Primary Health System's reporting entity because of the significance of their operational or financial relationships with the Primary Health System.

The primary mission of the Primary Health System and its component units is to provide healthcare services to the citizens of Chattanooga, Hamilton County and the surrounding area. Only those activities directly associated with this purpose are considered to be operating activities. Other activities that result in gains or losses unrelated to the Primary Health System's primary mission are considered to be nonoperating.

Erlanger Health Plan Trust, ContinuCare HealthServices, Inc., Cyberknife of Chattanooga, LLC, and UT-Erlanger Medical Group, Inc. are legally separate organizations which the Primary Health System has determined are component units of the Primary Health System.

Blended Component Unit: The financial statements of Erlanger Health Plan Trust include assets limited as to use totaling $1,637,342 as of June 30, 2017 and net investment gain totaling $6,003 for the year ended June 30, 2017 that are blended in the combined financial statements of the Primary Health System. The board of the Erlanger Health Plan Trust is substantially the same as that of the Primary Health System and the Primary Health System has operational responsibility.

Discretely Presented Component Units: The discretely presented component units' column in the combined financial statements includes the financial data of the Primary Health System's other component units. They are reported in a separate column to emphasize that they are legally separate from the Primary Health System. See the combined, condensed financial information in Note O.

1. ContinuCare HealthServices, Inc. and subsidiary (ContinuCare) provide health and supportive services to individuals in their homes in the Hamilton County and north Georgia areas. ContinuCare also provides retail pharmacy goods and services at four locations in Hamilton County. The Primary Health System owns 100% of the stock of ContinuCare. Separately audited financial statements for ContinuCare HealthServices, Inc. may be obtained by mailing a request to 1501 Riverside Drive, Suite 140, Chattanooga, Tennessee 37406.

2. Cyberknife of Chattanooga, LLC (Cyberknife) provides radiation therapy services, specifically robotic stereotactic radiosurgical services, through the use of a Cyberknife stereotactic radiosurgery system on the Primary Health System's campus. The Primary Health System owns 51% of Cyberknife's outstanding membership units and Cyberknife is fiscally dependent on the Primary Health System.

   A condition of admission as a Member of Cyberknife, is to deliver limited guaranties, guaranteeing pro-rata repayment of indebtedness of Cyberknife incurred to finance its equipment costs and its working capital needs. As of June 30, 2017, total debt outstanding was $1,312,500 with payments due through December 2018. Management believes that the Primary Health System will not be required to make any payments related to the guarantee of this indebtedness.

   Separate financial statements for Cyberknife of Chattanooga, LLC may be obtained by mailing a request to 975 East Third Street, Chattanooga, Tennessee 37403.

3. UT-Erlanger Medical Group, Inc. (the Medical Group) was formed on June 30, 2011 and will provide professional healthcare and related services to the public through employed and contracted licensed physicians and other supporting healthcare providers. The Medical Group has no members; however, the Primary Health System may access the Medical Group's services. The Primary Health System is not entitled to any potential earnings of the Medical Group except for compensation for services rendered to the Medical group on its behalf. However, based upon the significance of the Medical Group's potential operation to the Primary Health System, management believes its exclusion would be misleading and as such, includes the Medical Group as a component unit. The Medical Group is currently not active.

Erlanger Health System Foundations (the Foundation): The Foundation assists the Primary Health System to promote and develop charitable and educational opportunities as they relate to healthcare services provided by the Primary Health System. The Primary Health System is not financially accountable for the Foundation and as a result, the Foundation has not been included in the combined financial statements.

Contribution revenue from the Foundation totaling approximately $246,000 was recognized by the Primary Health System for the year ended June 30, 2017. The Primary Health System provided support to the Foundation of $987,000 in 2017.

Use of Estimates: The preparation of the combined financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the combined financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Enterprise Fund Accounting: The Primary Health System and its blended component units utilize the enterprise fund method of accounting whereby revenue and expenses are recognized on the accrual basis using the economic resources measurement focus.

Recently Issued Accounting Pronouncements: In June 2017, the GASB issued Statement No. 87, *Leases*, which requires balance sheet recognition of a liability and right-to-use asset for substantially all leases with a maximum possible term exceeding 12 months. The lease liability is measured at the present value of payments made during the lease term. In later periods, the lessee should amortize the discount of the lease liability and report it as an outflow of resources (interest expense) for the period. The lease asset is measured as the sum of the amount of the initial measurement of the lease liability, lease payments made to the lessor at/before the beginning of the lease term, and any initial direct costs. A lease asset is amortized over the shorter of the lease term or the useful life of the underlying asset and reported as an amortization expense. The requirements of this Statement are effective for reporting periods beginning after December 15, 2019; early adoption is permitted. Management is currently evaluating the impact of the adoption of the Statement on the combined financial statements.

Net Patient Service Revenue/Receivables: Net patient service revenue is reported on the accrual basis in the period in which services are provided at rates which reflect the amount expected to be collected. Net patient service revenue includes amounts estimated by management to be reimbursable by third-party payer programs under payment formulas in effect. Net patient revenue also includes an estimated provision for bad debts based upon management's evaluation of collectability based upon the age of the receivables and other criteria, such as payer classification and management's assumptions about conditions it expects to exist and courses of action it expects to take. The Primary Health System's policies do not require collateral or other security for accounts receivable, although the Primary Health System routinely accepts assignment or is otherwise entitled to receive patient benefits payable under health insurance programs, plans or policies. Supplemental payments from the State of Tennessee are recognized when determinable over the period to which they pertain (see Note B).

Charity Care: The Primary Health System accepts patients regardless of their ability to pay. A patient is classified as a charity patient by reference to certain policies established by the County Auditor with regard to the Hamilton County indigent program or by the Primary Health System for other patients. Essentially, these policies define charity services as those services for which minimal payment is anticipated. In assessing a patient's inability to pay, the County and the Primary Health System utilize the generally recognized poverty income levels, but also include certain cases where incurred charges are significant when compared to the income of the patient. These charges are not included in net patient service revenue.

Cash Equivalents: The Primary Health System considers all highly liquid investments with maturities of three months or less when purchased, excluding amounts whose use is limited by board designation, held by trustees under indenture agreement, or otherwise restricted as to use, to be cash equivalents.

Inventories: Inventories consist principally of medical and surgical supplies, general store supplies, and pharmacy items and are stated at lower of cost (first-in, first-out) or fair market value.

Investments: The Primary Health System's investments (including assets limited as to use) are reported at fair market value. Assets limited as to use include funds designated by the Board, funds held by trustees under trust indentures, and funds restricted by donors or grantors for specific purposes. The Primary Health System considers those investments with maturities of more than three months when purchased, maturing in more than one year and whose use is not limited by board designation, held by trustees under indenture agreement, or otherwise restricted as to use, to be long-term investments.

Temporary Investments: The Primary Health System considers all highly liquid investments with maturities of more than three months when purchased and maturing in less than one year, excluding amounts whose use is limited by board designation, held by trustees under indenture agreement, or otherwise restricted as to use, to be temporary investments.

Net Property, Plant and Equipment: Property, plant and equipment is recorded on the basis of cost. Donated assets are recorded at their fair market value at the date of donation. Leases that are substantially installment purchases of property are recorded as assets and amortized over the lesser of their estimated useful lives or the lease term which range from three to twenty years; related amortization is included in depreciation expense. Depreciation expense is computed over estimated service lives of the respective classes of assets using the straight-line method. The Primary Health System has established a capitalization threshold for property, plant and equipment of $2,500 except for computer equipment, which has a threshold of $1,000. Interest expense and interest income on borrowed funds related to construction projects are capitalized

during the construction period, if material. Costs of maintenance and repairs are charged to expense as incurred.

The Primary Health System reviews the carrying value of capital assets if facts and circumstances indicate that recoverability may be impaired. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. The Primary Health System did not experience any prominent events or changes in circumstances affecting capital assets which would require determination as to whether impairment of a capital asset has occurred during the year ended June 30, 2017.

Prepaid Bond Insurance: Costs related to insurance associated with bond issues are being amortized over the terms of the respective debt issues by the effective interest method.

Compensated Absences: The Primary Health System recognizes an expense and accrues a liability for employees' paid annual leave and short-term disability in the period in which the employees' right to such compensated absences is earned. Liabilities expected to be paid within one year are included as accrued salaries and related liabilities in the accompanying combined statements of net position.

Pensions: Pension amounts (net pension liability, deferred outflows of resources and deferred inflows of resources related to the pension, and pension expense, fiduciary net position of the Primary Health System's pension plan (the Plan) and additions to or deductions from the Plan's fiduciary net position) have been determined on the same basis as they are reported by the Plan. For this purpose, benefit payments are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Income Taxes: The Primary Health System is exempt from income taxes as it qualifies for exemption from federal income taxes pursuant to IRC Section 115 as an instrumentality of the State of Tennessee. Therefore, no provision for income taxes has been recognized in the accompanying combined financial statements for the Primary Health System.

As a for-profit entity, ContinuCare is subject to state and federal income taxes. ContinuCare HealthServices, Inc. and its subsidiary file consolidated federal income tax returns separately from the Primary Health System. At June 30, 2017, ContinuCare had no significant uncertain tax positions. Tax returns for the years ended June 30, 2014 through 2017 are subject to examination by taxing authorities.

As a limited liability corporation, Cyberknife, is subject to State of Tennessee income taxes. At June 30, 2017 Cyberknife had no significant uncertain tax positions. Tax returns for the years ended June 30, 2014 through 2017 are subject to examination by taxing authorities.

Contributed Resources: Resources restricted by donors for specific purposes are held as restricted funds and are recognized as operating or capital contributions in the accompanying combined financial statements. When an expense is incurred for purposes for which both restricted and unrestricted resources are available, restricted resources are used first. Fundraising expenses are netted against contributions recognized.

Net Position: The net position of the Primary Health System is classified into three components. *Net investment in capital assets* consists of capital and other assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. The *restricted expendable* net position consists of assets that must be used for a particular purpose that are either externally imposed by creditors, grantors, contributors or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation. *The unrestricted net position* consists of remaining assets that do not meet the definition of *net investment in capital assets* or *restricted expendable.*

Fair Value of Financial Instruments: The carrying amounts reported in the combined statements of net position approximate fair value, except as described below.

The carrying value of long-term debt and capital lease obligations (including the current portion) was $207,604,714 as of June 30, 2017. The estimated fair value of long-term debt and capital lease obligations (including current portion) was $213,110,000 at June 30, 2017. The fair value of long-term debt related to fixed interest long-term debt and capital lease obligations was estimated using discounted cash flows, based on the Primary Health System's incremental borrowing rates or from quotes obtained from investment advisors. The fair value of long-term debt related to variable rate debt approximates its carrying value.

NOTE B--NET PATIENT SERVICE REVENUE

A reconciliation of the amount of services provided to patients at established rates by the Primary Health System to net patient service revenue as presented in the combined statements of revenue, expenses and changes in net position for the year ended June 30, 2017 is as follows:

	Primary Health System
Inpatient service charges	$ 1,552,586,681
Outpatient service charges	1,307,574,226
Gross patient service charges	2,860,160,907
Less: Contractual adjustments and other discounts	1,792,010,245
Charity care	143,507,342
Provision for bad debts	89,121,349
	2,024,638,936
Net patient service revenue	$ 835,521,971

Charity Care and Community Benefit: The Private Act of the State of Tennessee establishing the Primary Health System obligates the Primary Health System to make its facilities and patient care programs available to the indigent residents of Hamilton County to the extent of funds appropriated by Hamilton County and adjusted operating profits, as defined. The annual appropriation from Hamilton County totaled $1,500,000 for fiscal year 2017. Total charity care charges for services provided to the certified indigent residents of Hamilton County (net of the appropriation) were approximately $16,554,000 for the year ended June 30, 2017 for the Primary Health System.

In addition to charity care provided to specific patients within the hospital setting, the Primary Health System also provides unreimbursed services to the community which includes free and low-cost health screenings. The Primary Health System also hosts health fairs and helps sponsor many other events that are free to the public and are spread throughout the year in various community locations.

The Primary Health System's Community Relations department includes HealthLink Plus, a free adult membership program with over 8,000 members in the Chattanooga Statistical Metropolitan Service Area. The Community Relations department hosts several free community events throughout the year utilizing the services of physicians, nurses, volunteers, educators, registered dietitians, social workers, secretaries and management personnel of the Primary Health System.

The Primary Health System's consumer call center, Erlanger HealthLink (423-778-LINK) is a free call center staffed by RN's to answer health questions, offer free physician referrals and to register participants in the programs offered by Community Relations, Women's & Infant Services and other departments and divisions of the Primary Health System.

Uncompensated Care Costs: The following table summarizes the estimated total uncompensated care costs (based on the ratio of total operating revenue and expenses) provided by Erlanger Medical Center as defined by the State of Tennessee for the year ended June 30, 2017:

Uncompensated cost of TennCare/Medicaid	$ 43,676,286
Traditional charity uncompensated costs	41,271,009
Bad debt cost	25,293,491
Total estimated uncompensated care costs	$ 110,240,786

The uncompensated cost of TennCare/Medicaid is estimated by taking the estimated cost of providing care to the TennCare/Medicaid patients less payments from the TennCare and Medicaid programs. The payments exclude revenues from essential access and other supplemental payments from TennCare of approximately $10,481,000 for the year ended June 30, 2017 and such payments are not guaranteed for future periods.

Revenue from Significant Payers: Gross patient service charges related to the Medicare program accounted for approximately 34.6% of the Primary Health System's patient service charges for the year ended June 30, 2017. Gross patient service charges related to the TennCare/Medicaid programs accounted for approximately 22.8% of the Primary Health System's patient service charges for the year ending June 30, 2017. TennCare typically reimburses providers at an amount less than their cost of providing services to TennCare patients. At June 30, 2017, the Primary Health System has a credit concentration related to receivables from the Medicare and TennCare programs.

During 2017, the Primary Health System recognized revenue related to trauma fund payments of approximately $1,170,000. Further, during 2017, the Primary Health System recognized disproportionate share payments (DSH) of approximately $8,620,000. Disproportionate share payments recognized in 2017 and prior years are subject to audit and potential recoupments although management believes it has meritorious defenses against any such recoupments. The U.S. District Court for the Middle District of Tennessee permanently enjoined the federal government from enforcing policies related to the calculation of the DSH payment limit against the Tennessee Hospital Association. The federal government has appealed this decision. Future distributions under these programs are not guaranteed. In 2017 the Primary Health System also received and recognized a net payment of $20,598,837 from the Public Hospital Supplemental Payment Pool. The Public Hospital Supplemental Payment Pool is part of the current Centers for Medicare and Medicaid Series pool methodology discussions.

Laws and regulations governing the Medicare and TennCare/Medicaid programs are complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates, as they relate to revenue recognized from these programs, will change by a material amount in the near term. The estimated reimbursement amounts are adjusted in subsequent

periods as cost reports are prepared and filed and as final settlements are determined. Final determination of amounts earned under prospective payment and cost reimbursement activities is subject to review by appropriate governmental authorities or their agents. Management believes that adequate provisions have been made for adjustments that may result from final determination of amounts earned under Medicare and Medicaid programs. The effect of prior year cost report settlements, or changes in estimates, had no significant impact on net patient service revenue in 2017.

The Primary Health System has also entered into reimbursement agreements with certain commercial insurance companies, health maintenance organizations and preferred provider organizations. The basis for reimbursement under these agreements includes prospectively determined rates, per diems and discounts from established charges.

NOTE C--CASH AND CASH EQUIVALENTS

Cash and cash equivalents reported on the combined statements of net position include cash on hand and deposits with financial institutions including demand deposits, which meet the definition of a cash equivalent.

Cash and cash equivalents consist of the following:

	Primary Health System
Demand deposits	$ 82,886,473
Cash on hand	14,454
	$ 82,900,927

Bank balances consist of the following:

	Primary Health System
Insured (FDIC)	$ 522,522
Collateralized under the State of Tennessee Bank Collateral Pool	86,154,815
	$ 86,677,337

In accordance with Tennessee Code Annotated Section 9-1-118, the full amount of principal and any accrued interest of each such deposit is insured by the FDIC up to statutory limits. For deposits above and beyond the amount covered by federal deposit insurance, the Primary Health

System follows the requirements as set forth in the Tennessee Code Annotated Title 9 Chapter 4, Part 5, "Collateral Pool for Public Deposits Act of 1990," whereby "Local governments with bank deposits that are in excess of the amount covered by FDIC insurance must either maintain the deposit with a bank that is a member of the bank collateral pool or collateralize the deposit in accordance with State statues."

The Primary Health System's deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized or are collateralized with securities held by the pledging financial institution's trust department or agent but not in the Primary Health System's name. The deposit risk is that, in the event of the failure of a depository financial institution, the Primary Health System will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. At June 30, 2017, the Primary Health System's bank balances were not exposed to custodial credit risk since the full amount was covered by FDIC insurance or by the State of Tennessee Collateral Pool.

NOTE D--DISAGGREGATION OF RECEIVABLE AND PAYABLE BALANCES

Patient Accounts Receivable, Net: Patient accounts receivable and related allowances are as follows:

	Primary Health System
Gross patient accounts receivable	$ 577,513,785
Estimated allowances for contractual adjustments and uncollectible accounts	(443,045,708)
Net patient accounts receivable	$ 134,468,077

Other Current Assets: Other current assets consist of the following:

	Primary Health System
Prepaid expenses	$ 6,920,287
Supplemental payments receivable (see Note B)	6,030,531
Other receivables	6,457,243
Total other current assets	$ 19,408,061

Accounts Payable and Accrued Expenses: Accounts payable and accrued expenses consist of the following:

	Primary Health System
Due to vendors	$ 72,812,098
Other	6,330,896
Total accounts payable and accrued expenses	$ 79,142,994

Other Long-Term Liabilities: Other long-term liabilities, and the related activity, consist of the following:

	Balance at June 30, 2016	*Unearned Revenue Recognized*	*Payments/ Other*	*Balance at June 30, 2017*
Compensated absences	$ 17,030,625	$ -	$ 2,872,242	$ 19,902,867
Medical malpractice	4,972,400	-	545,090	5,517,490
Job injury program	1,253,139	-	(1,096,798)	156,341
Unearned revenue	2,186,429	(237,858)		1,948,571
Other	89,760	-	-	89,760
Total other long-term liabilities	$ 25,532,353	$ (237,858)	$ 2,320,534	$ 27,615,029

NOTE E--NET PROPERTY, PLANT AND EQUIPMENT

Net property, plant and equipment activity for the Primary Health System consisted of the following:

	Balance at June 30, 2016	*Additions*	*Reductions/ Transfers*	*Balance at June 30, 2017*
Capital assets:				
Land and improvements	$ 21,569,286	$ 212,602	$ 1,965,112	$ 23,747,000
Buildings	233,712,632	629,412	32,727,123	267,069,167
Equipment	410,134,839	3,785,940	19,061,122	432,981,901
	665,416,757	4,627,954	53,753,357	723,798,068

	Balance at June 30, 2016	*Additions*	*Reductions/ Transfers*	*Balance at June 30, 2017*
Accumulated depreciation:				
Land and improvements	(8,825,770)	(559,962)	3,380	(9,382,352)
Buildings	(185,262,223)	(6,749,741)	40,518	(191,971,446)
Equipment	(334,925,533)	(19,022,818)	20,303,173	(333,645,178)
	(529,013,526)	(26,332,521)	20,347,071	(534,998,976)
Capital assets net of accumulated depreciation	136,403,231	(21,704,567)	74,100,428	188,799,092
Construction in progress	49,662,761	67,521,905	(74,466,368)	42,718,298
	$ 186,065,992	$ 45,817,338	$ (365,940)	$ 231,517,390

Construction in progress at June 30, 2017 consists of various projects for additions and renovations to the Primary Health System's facilities and computer systems. The estimated cost to complete construction projects is approximately $59,700,000. During 2017, the Primary Health System capitalized interest expense of approximately $3,300,000 on construction projects, net of interest income of approximately $300,000 earned on construction funds.

NOTE F--INVESTMENTS AND ASSETS LIMITED AS TO USE

The Primary Health System invests primarily in United States government and agency obligations, municipal and other bonds and short-term money market investments that are in accordance with the Primary Health System's investment policy. The carrying and estimated fair values for long-term investments, and assets limited as to use, by type are as follows:

	Primary Health System
U.S. Treasury notes	$ 38,870,890
U.S. Government agency obligations	69,298,329
Municipal bonds	9,799,690
Corporate bonds and others	4,151,705
Cash equivalents	10,395,768
Total investments and assets limited as to use	$ 132,516,382

Assets limited as to use are designated for the following purposes:

	Primary Health System
Capital investment funds	$ 107,521,078
Under bond indentures - held by trustees	
Debt service reserve fund	6,197,145
Construction fund	12,605,144
Self-insurance trust	4,057,659
Health plan trust	1,637,342
	$ 132,018,368

Assets limited as to use for capital investment are to be used for the replacement of property and equipment or for any other purposes so designated by the Board of Trustees. The debt service reserve fund is to be used only to make up any deficiencies in other funds related to the Hospital Revenue and Refunding Bonds Series 2004. The construction fund may be used for various construction and renovation projects related to the Series 2014 bonds.

The Primary Health System's investment policy specifies the types of investments which can be included in board-designated assets limited as to use, as well as collateral or other security requirements. The investment policy also specifies the maximum maturity of the portfolio of board-designated assets. Assets limited as to use and held by trustees are invested as permitted by the bond indenture.

Custodial Credit Risk: The Primary Health System's investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the name of the Primary Health System, and are held by either the counterparty or the counterparty's trust department or agent but not in the Primary Health System's name. The risk is that, in the event of the failure of the counterparty to a transaction, the Primary Health System will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. Substantially all of the Primary Health System's investments, including assets limited as to use, are uninsured or unregistered. Securities are held by the counterparty, or by its trust department or agent, in the Primary Health System's name.

Concentration of Credit Risk: This is the risk associated with the amount of investments the Primary Health System has with any one issuer that exceeds 5% or more of its total investments. Investments issued or explicitly guaranteed by the U.S. Government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement. The Primary Health System's investment policy does not restrict the amount that may be held for any single issuer. At June 30, 2017, none of the Primary Health System's

investments with any one issuer exceed 5% of its total investments except certain U.S. Government agency obligations.

Credit Risk: This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Primary Health System's investment policy provides guidelines for its fund managers and lists specific allowable investments. The credit risk profile of the Primary Health System's investments, including assets limited as to use (excluding U.S. Government securities), as of June 30, 2017, is as follows:

		Rating				
Investment Type	*Total*	*AAA*	*AA*	*A*	*BBB*	*N/A*
U.S. Government agency obligations	$ 69,298,329	$ 67,699,344	$ 1,598,985	$ -	$ -	$ -
Municipal bonds	9,799,690	5,407,178	4,172,437	220,075	-	-
Corporate bonds and others	4,151,705	2,949,881	-	1,201,824	-	-
Cash equivalents	10,395,768	-	-	-	-	10,395,768
Total investments	$ 93,645,492	$ 76,056,403	$ 5,771,422	$ 1,421,899	$ -	$ 10,395,768

Interest Rate Risk: This is the risk that changes in interest rates will adversely affect the fair value of an investment. The Primary Health System's investment policy authorizes a strategic asset allocation that is designed to provide an optimal return over the Primary Health System's investment horizon and within specified risk tolerance and cash requirements. The distribution of the Primary Health System's investments, including assets limited as to use, by maturity as of June 30, 2017, is as follows:

		Remaining Maturity				
Investment Type	*Total*	*12 months or less*	*13-24 Months*	*25-60 Months*	*Over 60 Months*	*N/A*
U.S. Treasury notes	$ 38,870,890	$ 1,235,437	$ 3,889,252	$ 33,746,201	$ -	$ -
U.S. Government agency obligations	69,298,329	14,033,987	7,260,921	1,694,965	46,308,456	-
Municipal bonds	9,799,690	7,565,872	2,019,310	214,508	-	-
Corporate bonds and others	4,151,705	1,217,071	-	2,934,634	-	-
Cash equivalents	10,395,768	10,395,768	-	-	-	-
Total investments	$ 132,516,382	$ 34,448,135	$ 13,169,483	$ 38,590,308	$ 46,308,456	$ -

NOTE G--LONG-TERM DEBT

Long-term debt at June 30, 2017 consists of the following:

	Primary Health System
Revenue and Refunding Bonds, Series 2014A, including bond premium of $7,929,184	$ 157,849,184
Revenue and Refunding Bonds, Series 2004, net of bond discount of $237,283 and including bond issue premium of $560,111	31,707,828
Total bonds payable	189,557,012
2014B Note payable	12,000,000
Capital leases - Note L	6,047,702
	207,604,714
Less: current portion	(4,686,080)
	$ 202,918,634

On December 1, 2014, the Primary Health System issued $149,920,000 Series 2014A bonds for the purpose of advance refunding $20,615,000 of the outstanding Series 2004 bonds (described below), $30,300,000 of the outstanding Series 2000 bonds, $17,375,000 of the Series 1998A bonds, and $27,465,000 of the outstanding Series 1997A bonds. The Primary Health System also utilized the proceeds to pay certain issuance costs and deposited a portion of the bond proceeds in the amount of $71,000,000 into a construction fund. The advance refunding of the Series 2004 bonds, Series 1998A bonds, and 1997A bonds resulted in a loss of $1,116,755 that is reported as a deferred outflow of resources and will be amortized over the term of the Series 2014A bonds.

The Series 2014A bonds consist of series bonds maturing annually beginning October 1, 2018 through 2034 and term bonds maturing on October 1, 2039 and 2044. The term bonds are subject to mandatory sinking fund redemption beginning October 1, 2035. The Series 2014A bonds are also subject to redemption by the Primary Health System at any interest payment date at a redemption price equal to the principal amount plus accrued interest.

Interest rates for the Series 2014A bonds are as follows:

Series bonds	3.0% to 5.0%
Term bonds	4.125% to 5.0%

In conjunction with the issuance of the Series 2014A bonds, the Primary Health Systems issued a $12,000,000 note payable (2014B note) through a financial institution to advance refund the remaining $11,775,000 of outstanding Series 1997A bonds and pay issuance costs. Principal payments of $100,000 are due annually beginning October 1, 2018 until the maturity date of October 1, 2021. The 2014B note bears interest, payable monthly, at a variable rate equal to the 1-month London Interbank Offered Rate plus a margin ranging from .73% to 2.25% based on the debt rating of the Primary Health System. The applicable interest rate at June 30, 2017 was 1.74%.

On January 1, 2004, the Primary Health System issued $85,000,000 insured Series 2004 bonds for the purpose of refunding $80,925,000 of the total outstanding Series 1993 bonds. The Primary Health System also utilized the proceeds to pay certain issuance costs and establish a debt service fund. The outstanding Series 2004 bonds mature annually on October 1 through 2022 in varying amounts. The Series 2004 bonds maturing after October 1, 2019 may be redeemed by the Primary Health System after October 1, 2019 at a redemption price equal to the principal amount plus accrued interest. Interest rates for the outstanding Series 2004 bonds range from 4.125% to 5.0%.

During 2015, a portion of the Series 2004 bonds totaling $20,615,000 were defeased with the issuance of the Series 2014A bonds proceeds through the deposit of funds into an irrevocable escrow account in amounts sufficient to pay the principal and interest when due. A portion of the defeased Series 2004 bonds totaling $10,840,000 has been redeemed. The escrow balance for payment of the remaining principal and interest totaled $10,440,718 at June 30, 2017.

The Series 2014A bonds, Series 2004 bonds and 2014B note were issued on parity, with respect to collateral, and are also secured by a mortgage on a portion of the Primary Health System's main campus. The trust indentures and related documents underlying the bonds contain certain covenants and restrictions. As of June 30, 2017, management believes the Primary Health System is in compliance with all such covenants.

Long-term debt activity for the Primary Health System for the year ended June 30, 2017 consisted of the following:

	Balance at June 30, 2016	*Additions/ Amortizations*	*Reductions/ Accretions*	*Balance at June 30, 2017*
Bonds Payable				
Series 2014	$ 158,140,163	$ -	$ 290,979	$ 157,849,184
Series 2004	36,183,687	68,759	4,544,618	31,707,828
Total bonds payable	194,323,850	68,759	4,835,597	189,557,012

	Balance at June 30, 2016	*Additions/ Amortizations*	*Reductions/ Accretions*	*Balance at June 30, 2017*
2014B Note payable	12,000,000	-	-	12,000,000
Other loans	188,397	-	188,397	-
Capital leases	6,217,356	-	169,654	6,047,702
Total long-term debt	$ 212,729,603	$ 68,759	$ 5,193,648	$ 207,604,714

The Primary Health System's scheduled principal and interest payments (estimated for variable rate debt based on rates at June 30, 2017) on bonds payable and other long-term debt (excluding capital leases) are as follows:

Year Ending June 30,	*Principal*	*Interest*	*Total*
2018	$ 4,575,000	$ 8,924,366	$ 13,499,366
2019	5,060,000	8,704,428	13,764,428
2020	5,295,000	8,463,545	13,758,545
2021	5,540,000	8,211,334	13,751,334
2022	5,815,000	7,933,911	13,748,911
2023-2027	24,780,000	36,362,243	61,142,243
2028-2032	28,265,000	31,217,008	59,482,008
2033-2037	35,985,000	23,331,484	59,316,484
2038-2042	45,225,000	13,877,425	59,102,425
2043-2045	32,765,000	2,511,125	35,276,125
TOTAL	$ 193,305,000	$ 149,536,869	$ 342,841,869

NOTE H--PENSION PLAN

Plan Description: The Primary Health System sponsors and administers the Chattanooga-Hamilton County Hospital Authority Pension Retirement Plan & Trust (the Plan), a single-employer, non-contributory defined benefit pension plan covering employees meeting certain age and service requirements. The Plan issues a publicly available financial report that can be obtained from 975 East Third Street, Chattanooga, Tennessee 37403.

The Primary Health System has the right to amend, in whole or in part, any or all of the provisions of the Plan. Effective July 1, 2009, the Plan was amended to be closed to new employees or rehires, and to further clarify the maximum years of service to be 30. During June 2014, the Plan was amended to freeze the accrual of additional benefits.

Benefits Provided: In addition to normal retirement benefits, the Plan also provides for early retirement, disability and death benefits. Retirement benefits are calculated as a percent of the employee's average monthly salary for the last 10 calendar years (prior to June 2014) times the employee's years of service. Employees earn full retirement benefits after 30 years of service. Early retirement benefits are available once an employee has reached age 55 and 10 years of service at a reduced rate based on age. Disability retirement benefits are available after 3 years of credited service, determined in the same manner as retirement benefits and are payable at the normal retirement date. Death benefits equal the actuarial equivalent value of the employee's vested accrued benefit as of the date of death. An employee who terminates service for other reasons after three years of credited service will receive retirement benefits at the normal retirement date.

Employees Covered: At July 1, 2017, the following employees were included in the Plan:

Active employees	1,814
Inactive employees with deferred benefits	1,294
Inactive employees currently receiving benefits	173
	3,281

Contributions: The Primary Health System has no legal or Plan requirements to fund the Plan and funds the Plan as contributions are approved by the Board of Trustees based on an actuarially determined rate recommended by an independent actuary. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned during the year with an additional amount to finance any unfunded accrued liability.

Net Pension Liability: The Primary Health System's net pension liability was measured as of June 30, 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of July 1, 2017. The total pension liability in the actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	N/A
Salary increases	N/A
Investment rate of return	7.5%
Discount rate	7.5%

The mortality assumption is based on the RP 2014 (adjusted to 2006) Total Data Set with Scale MP 2016.

The long-term expected rate of return on the Plan's investments was determined by applying the most recent capital market assumptions, as developed by the investment manager, using a building block approach. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized as follows:

Asset Class	*Target Allocation*	*Long-term Expected Real Rate of Return*
Large cap equity	15.00%	8.00%
Alternative investments	35.00%	7.00%
Mid/Small cap equity	10.00%	8.75%
International equity	20.00%	7.50%
Fixed income	15.00%	6.70%
Real estate	5.00%	7.00%

The Plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees assuming the actuarially determined contributions are made each year, although not required by the funding policy. Therefore, the discount rate for determining the total pension liability is equal to the long-term expected rate of return on pension plan investments.

Changes in the Net Pension Liability: Changes in the Primary Health System's net pension liability are as follows for the year ended June 30, 2017:

	Total Pension Liability	*Plan Fiduciary Net Position*	*Net Pension Liability*
Balance, June 30, 2016	$ 125,397,044	$ 58,558,658	$ 66,838,386
Interest	8,889,938	-	8,889,938
Liability gains or losses	4,595,946	-	4,595,946
Assumptions changes	1,015,446	-	1,015,446
Benefit payments	(13,981,845)	(13,981,845)	-
Administrative expenses	-	(518,260)	518,260
Investment income	-	4,052,889	(4,052,889)
Investment gains or losses	-	2,253,669	(2,253,669)
Employer contributions	-	5,550,488	(5,550,488)
Balance, June 30, 2017	$ 125,916,529	$ 55,915,599	$ 70,000,930

The following presents the net pension liability of the Primary Health System calculated using the current discount rate of 7.5 percent, as well as what the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.5%) or 1-percentage-point higher (8.5%) than the current rate:

	1% Decrease 6.5%	*Current Rate 7.5%*	*1% Increase 8.5%*
Net pension liability	$ 77,097,756	$ 70,000,930	$ 63,765,750

Pension Expense and Deferred Outflows of Resources: For the year ended June 30, 2017, the Primary Health System recognized pension expense totaling $9,484,103. At June 30, 2017, the Primary Health System reported deferred outflows of resources from the following sources:

	Deferred Outflows	*Deferred Inflows*
Differences between expected and actual experience	$ 5,543,929	$ -
Changes of assumptions	1,682,893	-
Differences between projected and actual earnings	4,802,736	-
	$ 12,029,558	$ -

Amounts reported as deferred outflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending June 30,	
2018	$ 4,128,799
2019	4,128,799
2020	3,376,827
2021	395,133

NOTE I--OTHER RETIREMENT PLANS

The Primary Health System maintains and administers defined contribution plans under Section 403(b) and 401(a) of the IRC which provides for voluntary contributions by employees. The Plans are for the benefit of all employees 25 years of age or older with at least 12 months of employment.

The Primary Health System matches 50% of each participant's contribution up to 2% of the participant's earnings. For eligible employees hired on or after July 1, 2009, the Primary Health System will make profit sharing contributions equal to 3% of their earnings, regardless if the

employee is making contributions. Additionally, active employees in the frozen pension plan will receive an additional 2.5% contribution through fiscal year 2019. Employer and employee contributions to the plans were approximately $1,870,000 and $9,724,000, respectively, for the year ended June 30, 2017.

NOTE J--MEDICAL MALPRACTICE AND GENERAL LIABILITY CLAIMS

As of January 1, 1976, the Primary Health System adopted a self-insurance plan to provide for malpractice and general liability claims and expenses arising from services rendered subsequent to that date. In 1980, the Primary Health System's Self-Insurance Trust Agreement (the Agreement) was amended to include all coverages that a general public liability insurance policy would cover. In 1988, the Agreement was amended and restated to comply with amendments to the Tennessee Governmental Tort Liability Act and to formally include any claims and expenses related to acts of employees of the Primary Health System. The Primary Health System is funding actuarial estimated liabilities through a revocable trust fund with a bank. The trust assets are included as a part of assets limited as to use in the accompanying combined statements of net position. Such amounts in the trust can be withdrawn by the Primary Health System only to the extent there is an actuarially determined excess. The annual deposit to the self-insurance trust fund is determined by management based on known and threatened claims, consultation with legal counsel, and a report of an independent actuary. Losses against the Primary Health System are generally limited by the Tennessee Governmental Tort Liability Act to $300,000 for injury or death to any one person in any one occurrence or $700,000 in the aggregate. However, claims against healthcare practitioners are not subject to the foregoing limits applicable to the Primary Health System. Any such individuals employed by the Primary Health System, excluding employed physicians for which the Primary Health System has purchased insurance coverage, are covered by the Trust to the limits set forth therein.

In the opinion of management, the revocable trust fund assets are adequate at June 30, 2017 to cover potential liability and malpractice claims and expenses that may have been incurred to that date.

The Primary Health System provides for claims and expenses in the period in which the incidence related to such claims occur based on historical experience and consultation with legal counsel. It is the opinion of management that the reserve for estimated losses and loss adjustment expense at June 30, 2017 is adequate to cover potential liability and malpractice claims which may have been incurred but not reported (IBNR) to the Primary Health System. Such reserve for IBNR claims reflects a discount rate of 5.5% based on the Primary Health System's expected investment return during the payout period.

NOTE K--COMMITMENTS AND CONTINGENCIES

Litigation: The Primary Health System is subject to claims and suits which arise in the ordinary course of business. In the opinion of management, the ultimate resolution of such pending legal proceedings has been adequately provided for in its combined financial statements, and will not have a material effect on the Primary Health System's results of operations or financial position.

Workers Compensation: The Primary Health System has a job injury program to provide benefits to workers injured in employment-related accidents. This program provides medical and indemnity benefits to employees injured in the course of employment for a period up to 24 months from the date of injury. The Primary Health System has recorded a projected liability for known claims that is included in other long-term liabilities in the combined statements of net position.

Healthcare Benefits: The Primary Health System maintains a self-insured healthcare plan to provide reimbursement for healthcare expenses for covered employees. The Primary Health System has estimated and recorded a liability for claims incurred but not reported in the combined financial statements.

Service Agreements: The Primary Health System has entered into various long-term service agreements. Early termination of the agreements could result in fees, penalties and reimbursement of various renovation expenses.

Electronic Health Records: The American Recovery and Reinvestment Act of 2009 and the Health Information Technology for Economic and Clinical Health (HITECH) Act established incentive payments under the Medicare and Medicaid programs for healthcare providers that use certified Electronic Health Record (EHR) technology. To qualify for incentive payments, healthcare providers must meet designated EHR meaningful use criteria as defined by the Centers for Medicare & Medicaid Services (CMS). Incentive payments are awarded to healthcare providers who have attested to CMS that applicable meaningful use criteria have been met. Compliance with meaningful use criteria related to amounts received and recognized in prior years is subject to audit by the federal government or its designee. Management believes the Primary Health System is in compliance with applicable rules and no accrual for repayment has been established.

Regulatory Compliance: The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services, Medicare fraud and abuse, and most recently under the Provision of Health Insurance Portability and Accountability Act of 1996, matters related to patient records, privacy and security. Recently, government activity has increased with

respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers, such as the Medicare Recovery Audit Contractor Program. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

In the normal course of business, the Primary Health System continuously monitors and investigates potential issues through its compliance program. Management believes that the Primary Health System is in compliance with applicable laws and regulations or has reported any amounts payable related to known violations, including amounts identified through the Medicare Recovery Audit Contractor program, or similar initiatives, and any settlements will not have a significant impact on the combined financial statements. However, due to the uncertainties involved and the status of ongoing investigations, management's estimate could change in the near future and the amount of the change could be significant.

Health Care Reform: In March 2010, Congress adopted comprehensive healthcare insurance legislation, Patient Care Protection and Affordable Care Act and Health Care and Education Reconciliation Act. The legislation, among other matters, is designated to expand access to coverage to substantively all citizens through a combination of public program expansion and private industry health insurance. Changes to existing TennCare and Medicaid coverage and payments are also expected to occur as a result of this legislation. Implementing regulations are generally required for these legislative acts, which are to be adopted over a period of years and, accordingly, the specific impact of any future regulations is not determinable.

Construction Grant: During 2017, the Primary Health System entered into an agreement with the Tennessee Valley Authority (TVA). Under the terms of the agreement, TVA will fund a portion of the cost of the construction of a new combined heat and power system (CHP), which will meet the technical requirements outlined in the agreement. The Primary Health System has committed to fund the remainder of the construction of the CHP (to be completed by June 2020) and to fund the operating costs of the CHP for a minimum of 12 years. The CHP is required to generate a specified level of output for 12 years subsequent to completion.

Payments to the Primary Health System are made by TVA based upon achieving certain milestones related to the construction of the CHP. During 2017, payments received totaled approximately $2,100,000 and have been recognized as part of capital contributions in the accompanying statements of changes in net position as management has determined this to be a nonexchange transaction and recognized the payments as milestones are achieved.

In the event the CHP is not completed and functional by June 30, 2020, the Primary Health System will be required to return all funds received. Further, in the event output over the 12-year period is less than specified in the agreement, the Primary Health System would be required to return a portion of the funds. Management believes the likelihood of any of the grant monies being repaid is remote based upon the progress to date and the heating and cooling requirements of the Primary Health System.

Letter of Intent: On June 23, 2017, the Primary Health System entered into a Letter of Intent ("LOI") with the current member/operator of Murphy Medical Center ("Hospital"), Town of Murphy Hospital, Southwestern Health System, Inc., and Murphy Medical Center, Inc., for the purpose of exploring partnership opportunities between Primary Health System and the Hospital in Murphy, NC. Currently, the Primary Health System, through a due diligence process, is considering a member substitution scenario versus a lease arrangement. In the member substitution scenario, the Primary Health System would assume the assets and liabilities. In the lease scenario, the Primary Health System would lease the Hospital for an amount certain. Under both scenarios, the Primary Health System would be responsible for the ongoing operations of the Hospital on a go forward basis. Per the LOI, the parties expect to complete the due diligence process and, if to the Primary Health System's satisfaction, execute a definitive agreement prior to January 1, 2018.

Behavioral Health Joint Venture: Through a joint venture with Acadia Chattanooga Holdings, LLC, via articles of organization filed with the Secretary of State's office on March 7, 2016, the Primary Health System became a minority owner in Erlanger Behavioral Health, LLC, a Tennessee, limited liability company, formed for the purpose of constructing and operating an inpatient and outpatient behavioral health hospital in Chattanooga, Tennessee. In exchange for a 20% ownership in the venture, the Primary Health System contributed the costs for obtaining and the associated value of the appropriate certificate of need, twelve existing geri-psych beds previously housed at its North facility, its trade name and mark, and a contribution toward the option for the purchase of real property upon which the project will be housed. The project is currently under construction and expected to be accepting patients in the spring of 2018. The Health System does not guarantee any indebtedness or have any other financial obligations related to the entity.

NOTE L--LEASES

Capital: During 2012, the Primary Health System entered into an agreement to sell certain professional office buildings (POBs) and concurrently entered into agreements to lease space from the purchaser. The sales price of the POBs was approximately $13,333,000, and a gain of approximately $6,695,000 was realized. Since the Primary Health System is leasing back certain space, a portion of the gain has been deferred and is being recognized over the terms of the

leases. Amortization of the deferred gain is included in non-operating revenue (expenses) for the year ended June 30, 2017. The leases entered into under this sale/leaseback agreement include certain leases which meet the criteria for capitalization. Interest on these leases has been estimated at 7% per annum.

During 2011, the Primary Health System acquired a parcel of land from the Industrial Development Board of the City of Chattanooga, Tennessee for a nominal amount. The Primary Health System also entered into a project development agreement with a developer to facilitate final design, financing and construction of a medical office building for the benefit of Volkswagen Group of America Chattanooga Operations, LLC (Volkswagen) on this land. The Primary Health System has entered into a forty-year ground lease, with the option of two ten-year renewal terms, of the parcel to the developer. Additionally, in 2012, the Primary Health System has entered into a twenty-year lease with the developer for certain space in the medical office building for a wellness center and other operations under a capital lease agreement.

The following is a summary of the net book value of property under capital leases by major classes at June 30, 2017:

	Primary Health System
Buildings	$ 6,599,976
Equipment	79,333
	6,679,309
Less: accumulated amortization	(2,432,777)
	$ 4,246,532

The following is a schedule of future minimum lease payments under capital leases:

Year Ending June 30,	
2018	$ 744,453
2019	759,311
2020	774,587
2021	790,291
2022	806,435
2023-2027	3,622,896

Year Ending June 30,	
2028-2032	3,527,970
2033-2034	160,498
Total minimum lease payments	11,186,441
Less: amount representing interest	(5,138,739)
Present value of minimum lease payments	$ 6,047,702

Operating: The Primary Health System rents office space and office equipment under non-cancelable operating leases through 2033, containing various lease terms. The leases have other various provisions, including sharing of certain executory costs. Rent expense under operating leases was approximately $16,770,000 in 2017.

Future minimum lease commitments for all non-cancelable leases with terms in excess of one year are as follows:

Year Ending June 30,	
2018	$ 12,735,282
2019	9,470,716
2020	7,658,897
2021	4,625,853
2022	1,628,423
Thereafter	17,402,053
	$ 53,521,224

Rental Revenues: The Primary Health System leases office space to physicians and others under various lease agreements with terms in excess of one year. Rental revenue recognized for the year ended June 30, 2017 totaled approximately $2,901,000. The following is a schedule of future minimum lease payments to be received:

Year Ending June 30,	
2018	$ 1,050,500
2019	372,645
2020	224,978
2021	86,118
2022	60,451
Thereafter	226,836
	$ 2,021,528

NOTE M--FAIR VALUE MEASUREMENTS

The Primary Health System categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets or liabilities; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

The Primary Health System has the following recurring fair value measurements as of June 30, 2017:

	Carrying Value	*Level 1*	*Level 2*	*Level 3*
U.S. Treasury obligations	$ 38,870,890	$ 38,870,890	$ -	$ -
U.S. government agency obligations	69,298,329	-	69,298,329	-
Municipal bonds	9,799,690	-	9,799,690	-
Corporate bonds and others	4,151,705	-	4,151,705	-
Cash and cash equivalents	10,395,768	10,395,768	-	-
	$132,516,382	$ 49,266,658	$ 83,249,724	$ -

The fair value of investments in U.S. government agency bonds, municipal bonds and corporate bonds is estimated based on matrix pricing of similar assets or market corroborated pricing.

NOTE N--MANAGEMENT AGREEMENT

On April 13, 2011, the Primary Health System's Board of Trustees approved a resolution authorizing a management agreement (the Agreement) between the Primary Health System, Hutcheson Medical Center, Inc. and affiliates (collectively, Hutcheson) and the Hospital Authority of Walker, Dade and Catoosa Counties in Georgia (the Hospital Authority).

Under the terms of the Agreement, the Primary Health System proposed general operating policies and directives for Hutcheson; was responsible for the day-to-day management of Hutcheson and provided oversight of ancillary aspects of Hutcheson, such as physician practices, education, research, and clinical services. The Agreement's initial term was to be through March 31, 2021 with the Primary Health System to have the option to extend the agreement for two additional five-year terms. The Primary Health System was authorized to terminate the Agreement, without cause, upon written notice at any point subsequent to May 25, 2013. Upon such termination, Hutcheson was to be obligated to make a Termination Payment to the Primary Health System consisting of all expenses then owed by Hutcheson and any outstanding advances under a Line of Credit Agreement, discussed below. Hutcheson could also terminate the agreement without cause at any point subsequent to May 25, 2013 by paying the Termination

Payment, as well as the lesser of a) $1,000,000 per year for each year the Agreement has been in place, or b) $1,000,000 less any management fees paid in each Agreement year.

In addition to the Agreement, the Primary Health System agreed to extend a Line of Credit (the Line) to the Hospital Authority. The maximum amount available under the Line was $20,000,000 and at June 30, 2017, the draws on the Line totaled $20,000,000. The Line called for interest only payments each month on the outstanding balance, based on the London InterBank Offered Rate plus 4% or a rate of 5%, whichever is greater. However, any unpaid interest through March 31, 2013 was deferred and to be paid over a twelve-month period commencing on that date. All outstanding draws were due at the maturity date, which is consistent with the Agreement termination dates, discussed above.

The Line was secured by a Security Agreement on the primary Hutcheson medical campus. Further, the Counties of Walker and Catoosa, Georgia (collectively, the Counties) provided additional security in the form of guarantees under an Intergovernmental Agreement. Under the Intergovernmental Agreement, the Counties each agreed to a maximum liability of $10,000,000 to secure the line. The form of such guarantee was at the option of the Counties and was to become enforceable upon a notice of default delivered by the Primary Health System. The form of the guarantee selected by the Counties can include a) a payment of 50% by each County of the amounts owing under the Line, b) payments as they become due up to the respective $10,000,000 limits or c) after non-Judicial foreclosure under the Security Agreement, each County could elect to pay 50% of any deficiency between the amount outstanding under the Line and the then fair market value. Both Counties previously agreed to levy annual property taxes, if needed to honor these guarantees.

In June 2013, the Agreement was modified to allow Hutcheson to issue requests for proposals for the lease or sale of Hutcheson properties without creating a breach of the Agreement. As part of the Agreement, Hutcheson committed to obtain alternative financing and repay the line of credit upon the earlier of the replacement financing being obtained by Hutcheson, or June 1, 2014. In August of 2013, however, Hutcheson terminated the Agreement. In response thereto, the Primary Health System declared Hutcheson to be in default under the Agreement and made formal demand of Hutcheson as to all amounts then due and payable. In February 2014, the Primary Health System filed suit against Hutcheson in order to collect the moneys, including principal, interest and penalties, then due. In response to such filing, Hutcheson has asserted multiple counter claims against the Primary Health System alleging mismanagement and other failures under the Agreement. Additionally, another senior creditor has filed a separate lawsuit against the Primary Health System alleging priority over the Primary Health System's security interest and, presumably, the County guarantees relating to Hutcheson. The litigation was filed in the United States District Court in the Northern District of Georgia, Rome Division.

During the pendency of the litigation, Hutcheson's operating entities (Hutcheson Medical Center, Inc. and Hutcheson Medical Division, Inc., but not the Hospital Authority) filed for Chapter 11 bankruptcy protection in the Northern District of Georgia. Such filing automatically stayed the pending litigation to the extent it pertained to Hutcheson's operating entities. On September 15, 2015, the Bankruptcy Court did appoint a Chapter 11 Trustee in order to facilitate a sale of Hutcheson's interests and to consider conversion to a Chapter 7 under the Bankruptcy Code. Following the filing of adverse proceedings by the Primary Health System against the Hutcheson entities with the Bankruptcy Court, the parties reached an agreement as to the sale and disposition of the entities' primary assets, including its skilled nursing facility and acute care hospital. As a result of the same, the Primary Health System was paid a total of $2,590,000 from such sale and, further, the Bankruptcy Court made various findings of fact to enable the Primary Health System to pursue its guarantees against Walker and Catoosa County. Per the Agreement and the Line, the Counties were entitled to and did receive a credit against their guarantees. The Primary Health System remains tangentially involved in the bankruptcy action to ensure that any of its interests remain adequately protected. That portion of the litigation relating to the Hospital Authority, which is unable to seek bankruptcy protection under Georgia law, did continue for a period of time parallel to the bankruptcy proceeding and ultimately resulted in judgment in the Primary Health System's favor in the amount of $36,500,000. The Hospital Authority is apparently judgment-proof and has no material assets at this point. The Primary Health System remains a judgment creditor against the Hospital Authority.

Regions Bank (Regions) is also a creditor of Hutcheson and initiated related litigation in the U.S. District Court for the Northern District of Georgia in Rome (Case No. 4:14-cv-00191) against the Primary Health System in its effort to protect its interest, if any, in the litigation. Specifically, Regions claims the Primary Health System's interest is subordinate to its interest and seeks a declaration of such priority. Regions claims that Hutcheson owes Regions in excess of $22.3 million that is allegedly a senior debt to the debt Hutcheson owes to the Primary Health System. Regions further claims that the Primary Health System's attempted foreclosure constitutes a breach of the Management Agreement to which Regions is allegedly a third-party beneficiary and related contracts. Regions filed a Motion for a temporary restraining order on July 28, 2014, seeking to enjoin the foreclosure proceedings. The Court denied Regions Motion for a temporary restraining order as moot in light of the injunctive relief it granted to Hutcheson in the related litigation. Regions filed a second Motion for a temporary restraining order on October 15, 2014, which was heard on October 24, 2014. The Court again denied the Motion for a temporary restraining order as moot due to the injunctive relief granted to Hutcheson in the related litigation. The Primary Health System filed a Motion to Dismiss in the Regions suit, which was granted on October 29, 2014 and dismissed all claims against the Primary Health System in their entirety. Regions appealed the dismissal to the 11th Circuit. As part of the agreement reached in the adverse action filed by the Primary Health System in the Bankruptcy Court (as referenced above), Regions agreed to dismiss its appeal with prejudice.

On or about December 28, 2015, Erlanger filed suit against Walker County in the United States District Court for the Northern District of Georgia in Rome (Case No. 4:15-cv-00250) to enforce its guarantee on the remaining amount of approximately $8,705,000 (in consideration of the credit referenced above), plus interest. On August 23, 2016, the Court granted the Primary Health System's motion for summary judgment for such amount. Shortly thereafter, Walker County appealed that order to the 11th Circuit Court of Appeals, which court affirmed on all counts July 17, 2017. The Court of Appeals thereafter remanded the case back to the Court for trial on the issue of attorneys' fees owed to the Primary Health System relating to the litigation. The pre-trial scheduling order is currently due on September 28, 2017. The Primary Health System intends to seek enforcement of the Court's judgment as to principal, interest and attorneys' fees immediately. At June 30, 2017, amounts due from Walker County are reflected as current or long-term assets based on management's evaluation of the timing of payments.

As to Catoosa County, rather than file suit directly against it, the Primary Health System worked with and negotiated a settlement agreement resolving all claims under the guarantee as to Catoosa County for the lump-sum payment of $6,250,000. Such amounts were paid in full in 2016.

NOTE O--CONDENSED FINANCIAL INFORMATION

The following is condensed, financial information related to the discretely presented component units as of and for the year ended June 30, 2017:

	ContinuCare	*Cyberknife*
Due from other governments	$ 247,615	$ 177,004
Other current assets	20,757,822	370,212
Total Current Assets	21,005,437	547,216
Net property, plant and equipment	4,573,500	2,459,249
Other assets	467,177	41,420
Total Assets	$ 26,046,114	$ 3,047,885
Due to other governments	$ 1,199,599	$ -
Other current liabilities	6,724,038	480,302
Total Current Liabilities	7,923,637	480,302
Long-term debt and capital lease obligations	718,454	937,500
Total Liabilities	8,642,091	1,417,802

	ContinuCare	*Cyberknife*
Net position		
Unrestricted	12,833,343	441,914
Net investment in capital assets	4,570,680	1,188,169
Total Net Position	17,404,023	1,630,083
Total Liabilities and Net Position	$ 26,046,114	$ 3,047,885
Year Ended June 30, 2017		
Net patient and operating revenue	$ 32,364,798	$ 1,838,267
Operating expenses:		
Salaries, wages and benefits	14,697,033	258,582
Supplies and other expenses	21,093,742	646,969
Depreciation	609,519	628,590
Total Operating Expenses	36,400,294	1,534,141
Operating Income (Loss)	(4,035,496)	304,126
Nonoperating revenue (expense)	6,796,216	(81,423)
Operating distributions	-	(250,000)
Change in Net Position	2,760,720	(27,297)
Net Position at Beginning of Period	14,643,303	1,657,380
Net Position at End of Period	$ 17,404,023	$ 1,630,083

ContinuCare owes the Primary Health System for various services, supplies, and rents provided, or expenses paid on its behalf. Actual expenses incurred related to these services (including 340(b) pharmacy discounts remitted to the Primary Health System) were approximately $7,612,000 in 2017. In addition, ContinuCare provides staffing, contract nurse visits, and administrative services to the Primary Health System. Revenues from such services were approximately $584,000 for the year ended June 30, 2017. Amounts due at June 30, 2017 are included in amounts due to/from other governments in the accompanying combined financial statements. During 2017, ContinuCare sold substantially all of its pharmacy operations to an unrelated third party. A gain of approximately $8,000,000 was recognized on the sale of the operations and assets.

The Primary Health System owes Cyberknife for radiation services provided by Cyberknife to the Primary Health System's patients. Revenues related to those services provided to the Primary Health System were approximately $1,840,000 in 2017. Amounts due at June 30, 2017 are included in amounts due to/from other governments in the accompanying combined financial statements.

NOTE P--SUBSEQUENT EVENTS

Subsequent events have been evaluated through the date of the Independent Auditor's Report, which is the date the financial statements were available to be issued. During this period, management did not note any material recognizable subsequent events that required recognition or disclosure in the June 30, 2017 financial statements.

REQUIRED SUPPLEMENTARY INFORMATION

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Schedule of Changes in Net Pension Liability and Related Ratios

Year Ended June 30, 2017

	2016	2017
Total pension liability		
Interest	$ 9,054,674	$ 8,889,938
Differences between expected and actual experience	3,599,202	4,595,946
Changes of assumptions or inputs	(329,629)	1,015,446
Benefit payments	(15,040,450)	(13,981,845)
Net change in total pension liability	(2,716,203)	519,485
Total pension liability, beginning of year	128,113,247	125,397,044
Total pension liability, end of year	$ 125,397,044	$ 125,916,529
Plan fiduciary net position		
Contributions - employer	$ 2,000,004	$ 5,550,488
Net investment income, net	(4,064,193)	6,306,558
Benefit payments	(15,040,450)	(13,981,845)
Administrative expense	(592,487)	(518,260)
Net change in plan fiduciary net position	(17,697,126)	(2,643,059)
Plan fiduciary net position, beginning of year	76,255,784	58,558,658
Plan fiduciary net position, end of year	$ 58,558,658	$ 55,915,599
Net pension liability, end of year	$ 66,838,386	$ 70,000,930
Fiduciary net position as a percentage of the total pension liability	46.70%	44.41%
Covered payroll	$ 117,027,000	$ 106,620,000
Net pension liability as a percentage of covered payroll	57.11%	65.65%

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Schedule of Actuarial Contributions

Year Ended June 30, 2017

	2017	*2016*	*2015*	*2014*	*2013*	*2012*	*2011*	*2010*	*2009*	*2008*
Actuarially determined contributions	$ 5,943,258	$ 4,957,642	$ 4,364,255	$ 12,832,292	$ 11,165,101	$ 10,367,973	$ 8,833,977	$ 7,501,004	$ 7,192,948	$ 6,731,386
Actual employer contributions	5,550,488	2,000,004	1,000,000	-	11,165,101	10,367,970	8,833,977	7,501,004	7,192,000	6,172,593
Contribution deficiency	$ 392,770	$ 2,957,638	$ 3,364,255	$ 12,832,292	$ -	$ 3	$ -	$ -	$ 948	$ 558,793
Covered payroll	$ 106,619,652	$ 117,026,565	$ 115,717,311	$ 121,093,695	$ 138,807,819	$ 147,947,134	$ 144,176,724	$ 139,291,860	$ 138,478,848	$ 127,662,977
Contributions as a percentage of covered payroll	5.21%	1.71%	0.86%	0.00%	8.04%	7.01%	6.13%	5.39%	5.19%	4.84%

Notes to Schedule:

Valuation date:	Actuarially determined contribution rates are calculated as of June 30, one year prior to the end of the fiscal year in which contributions are reported.
Actuarial cost method:	Entry age normal
Amortization method:	Level dollar, closed
Amortization period:	18 years
Asset valuation method:	4-year smoothed market
Inflation:	N/A
Lump sum interest rate:	4.0%
Salary increases:	N/A
Investment rate of return:	7.25%
Retirement age:	Normal retirement at 65 years, early retirement at 55 years with 10 years of service
Mortality:	RP 2014 (adjusted to 2006) Total Data Set with Scale MP 2016 in 2017 RP-2014 Mortality for Employees, Health Annuitants, and Disabled Annuitants with general projection per MP-2015 in 2016 RP-2014 Mortality for Employees, Health Annuitants, and Disabled Annuitants with general projection per MP-2014 in 2015 RP-2000 Mortality for Employees, Health Annuitants, and Disabled Annuitants projected to 2018 per Scale AA in 2014

SECTION III

INTERNAL CONTROL AND COMPLIANCE SECTION

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of
Chattanooga-Hamilton County Hospital Authority
(d/b/a Erlanger Health System):

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the combined financial statements of the business-type activities and the aggregate discretely presented component units of Chattanooga-Hamilton county Hospital Authority d/b/a Erlanger Health System (the Primary Health System) as of and for the year ended June 30, 2017, and the related notes to the combined financial statements, which collectively comprise the Primary Health System's basic combined financial statements, and have issued our report thereon dated September 20, 2017

Internal Control Over Financial Reporting

In planning and performing our audit of the combined financial statements, we considered the Primary Health System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the combined financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Primary Health System's internal control. Accordingly, we do not express an opinion on the effectiveness of the Primary Health System's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Primary Health System's combined financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Primary Health System's combined financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of the Primary Health System's combined financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Primary Health System's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Primary Health System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Pershing Yoakley & Associates PC

Knoxville, Tennessee
September 20, 2017

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Schedule of Expenditures of Federal Awards

Year Ended June 30, 2017

Grantor	*Pass-Through Grantor Agency*	*Program Name*	*CFDA Number*	*Grant Number (Grant Period)*	*Federal Expenditures*
U.S. Department of Agriculture	Chattanooga-Hamilton County Health Department	Special Supplemental Nutrition Program for Women, Infants, and Children	10.557	GG-15-43883-00 (10/1/15 - 9/30/17)	$ 77,176
U.S. Department of Health and Human Services	N/A	Health Center Program (Community Health Centers)	93.224	H80CS00091 (12/1/01 - 3/31/2020)	3,533,067
U.S. Department of Health and Human Services	State of Tennessee Department of Health Bureau of TennCare	High Risk Perinatal Program	93.778	GG-15-45987-01 (7/1/15-6/30/18)	479,720
U.S. Department of Health and Human Services	State of Tennessee Department of Health	Maternal and Child Health Services Block Grant to the States	93.994	GG-15-42120-00 (7/1/14-6/30/17)	20,334
U.S. Department of Health and Human Services	State of Tennessee Department of Health	Maternal and Child Health Services Block Grant to the States	93.994	GG-15-42431-00 (7/1/14-6/30/17)	249,249
				Total U.S. Department of Health and Human Services	4,282,370
				Total Expenditures of Federal Awards	$ 4,359,546

See notes to schedules of expenditures of federal awards and state and other financial assistance.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Schedule of Expenditures of State and Other Financial Assistance

Year Ended June 30, 2017

Grantor	*Program Name*	*Contract Number (Contract Period)*	*Beginning Balance*	*Cash Received*	*Grant Expenditures (Adjustments)*	*Ending Balance*
State of Tennessee Department of Health, Bureau of TennCare	High Risk Perinatal Program	GG-15-45987-00 (7/1/15 - 6/30/18)	$ 97,676	$ 97,666	$ (10)	$ -
		GG-15-45987-01 (7/1/15 - 6/30/18)	-	316,107	479,730	163,623
State of Tennessee Department of Health	Maternal and Child Health Services Block Grant to the States	GG-15-42935-00 (7/1/14 - 6/30/19)	5,200	28,600	28,600	5,200
		GG-14-42431-00 (7/1/14 - 6/30/17)	15,981	43,837	51,051	23,195
		GG-15-42120-00 (7/1/14 - 6/30/17)	2,156	8,408	7,521	1,269
State of Tennessee Department of Health	Infant Mortality Perinatal Simulation Services	GC-15-45374-00 (4/1/15 - 6/30/15)	(6,804)	-	-	(6,804)
State of Georgia Department of Community Health	Life Force Air Ambulance Grant	12002G (7/1/16 - 6/30/17)	-	600,000	600,000	-
	TOTAL STATE AND OTHER FINANCIAL ASSISTANCE		$ 114,209	$ 1,094,618	$ 1,166,892	$ 186,483

See notes to schedules of expenditures of federal awards and state and other financial assistance.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Notes to Schedules of Expenditures of Federal Awards and State and Other Financial Assistance

Year Ended June 30, 2017

NOTE A--BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards and schedule of expenditures of state and other financial assistance include the grant activity of Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System (the Primary Health System) and are presented on the accrual basis of accounting. The information in these schedules is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) and the Tennessee Comptroller of the Treasury, respectively. Therefore, some amounts presented in these schedules may differ from amounts presented in, or used in the preparation of, the basic combined financial statements.

NOTE B--SIGNIFICANT ACCOUNTING POLICIES

De Minimis Indirect Cost Rate: The Primary Health System has elected not to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance.

NOTE C--CONTINGENCIES

The Primary Health System's federal programs are subject to financial and compliance audits by grantor agencies which, if instances of material noncompliance are found, may result in disallowed expenditures and affect the Primary Health System's continued participation in specific programs. The amount, if any, of expenditures which may be disallowed by the grantor agencies cannot be determined at this time, although the Primary Health System expects such amounts, if any, to be immaterial.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Schedule of Findings and Questioned Costs

Year Ended June 30, 2017

Section I - Summary of Auditor's Results

FINANCIAL STATEMENTS

The auditor's report expressed an unmodified opinion on the combined financial statements of Chattanooga-Hamilton County Hospital Authority.

Internal control over financial reporting:	
Material weakness(es) identified?	Yes [ ] No [X]
Significant deficiency identified?	None Reported
Noncompliance material to combined financial statements noted?	Yes [ ] No [X]

FEDERAL AWARDS

The auditor's report on compliance for the major federal award programs for Chattanooga-Hamilton County Hospital Authority expresses an unmodified opinion on its major federal programs.

Internal control over major programs:	
Material weakness(es) identified?	Yes [ ] No [X]
Significant deficiency identified?	None Reported
Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	Yes [ ] No [X]

Identification of Major Programs:

CFDA Number(s)	*Name of Federal Program or Cluster*
93.224	U.S. Department of Health and Human Services – Health Center Program (Community Health Centers)

Dollar threshold used to distinguish between Type A and Type B programs:	$ 750,000
Auditee qualified as low-risk auditee?	Yes [X] No [ ]

Section II - Financial Statement Findings

This section identifies the significant deficiencies, material weaknesses, fraud, illegal acts, violations of provisions of contracts and grant agreements, and abuse related to the combined financial statements for which *Government Auditing Standards* require reporting.

Not applicable, no financial statement findings.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Schedule of Findings and Questioned Costs - Continued

Year Ended June 30, 2017

Section III - Federal Award Findings and Questioned Costs

In this section, the auditor should only identify the audit findings that are required to be reported in 2CFR200 Section 516(a) of the Uniform Guidance (i.e., significant deficiency, material weakness, or material instances of noncompliance, and any related questioned costs), as well as any abuse findings involving federal awards that are material to a major program. Furthermore, each finding should be organized by particular federal agency or pass-through entity, to the extent practical.

Not applicable, no findings or questioned costs.

CHATTANOOGA-HAMILTON COUNTY HOSPITAL AUTHORITY
(d/b/a Erlanger Health System)

Schedule of Prior Audit Findings

Year Ended June 30, 2017

There were no prior audit findings.

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REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH UNIFORM GUIDANCE

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees of
Chattanooga-Hamilton County Hospital Authority
(d/b/a Erlanger Health System):

Report on Compliance for Each Major Federal Program

We have audited Chattanooga-Hamilton County Hospital Authority d/b/a Erlanger Health System's (the Primary Health System) compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget Compliance Supplement* that could have a direct and material effect on each of the Primary Health System's major federal programs for the year ended June 30, 2017. The Primary Health System's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Primary Health System's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Primary

Health System's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Primary Health System's compliance.

Opinion on Each Major Federal Program

In our opinion, the Primary Health System complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2017.

Report on Internal Control Over Compliance

Management of the Primary Health System is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Primary Health System's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Primary Health System's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that were not identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Pershing Yoakley & Associates PC

Knoxville, Tennessee
January 8, 2018